In the

Supreme Court of the United States

October Term, 1937

No. 55

MARY DUKE BIDDLE,

Petitioner,

against

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF OF AMICI CURIAE

INDEX

	PAGE
REASONS FOR FILING BRIEF	1
THE ISSUE AND THE PRECEDENTS	2
The Question	2
The Precedents	2
Administrative Practice	2
Circuit Court Decisions	3
SUMMARY OF ARGUMENT	5
Argument	6
POINT A. Under the British Tax System the Shareholder Pays the Tax Deducted and Withheld on the Payment of a Dividend	6
1. The British System of Taxation	6
2. Taxation of Dividends	9
3. Neumann v. Commissioners of Inland Revenue	14
4. British Administrative Practice	17
POINT B. The Broad Relief Purposes of the Statute Require That the Credit be Allowed	20
CONCLUSION	26

UNITED STATES CITATIONS

Cases

Burnett v. *Chicago Portrait Co.*, 285 U. S. 1, 76 Law Ed. 587	20
George W. Elkins v. *Commissioner*, 91 Fed. (2d) 534	4
Shearer v. *Commissioner*, 48 F. (2d) 552	26
United Dyewood Corporation v. *Bowers*, 56 Fed. (2d) 603	27
United Shoe Machinery Corporation v. *White, Collector, etc.*, 89 Fed. (2d) 363	4
Welch, Collector v. *St. Helens Petroleum Co., Ltd.*, 78 Fed. (2d) 631	3
F. W. Woolworth Co. v. *United States*, 91 Fed. (2d) 973	1, 3

Miscellaneous

PAGE

Article 143-9, Regulations 94, Income Tax..... 27

Section 213 (b) 14 of the Revenue Act of 1926... 22

Section 103, Revenue Act of 1936 25

Section 22 (b) of the Revenue Act of 1936..... 24

House Report No. 350, 67th Congress, 1st Session 23

Preliminary Report of the Subcommittee on Ways and Means, 73rd Congress, 2nd Session..... 23

Convention and Protocol with France 24

Reciprocal Convention between United States and Canada 25

Cases

BRITISH CITATIONS

Attorney-General v. *Ashton Gas Company,* (1906) A. C. 10, (Referred to in quotation.) 12

Blott v. *Commissioners of Inland Revenue,* (1921) 2 A. C. 171 (Referred to in quotation.) 13

Brooke v. *Commissioners of Inland Revenue,* (1918) 1 K. B. 257; 7 Tax Cases 261. (Referred to in quotation.) 12

F. H. Hamilton v. *Commissioners of Inland Revenue,* (1931) 2 K. B. 495; 16 Tax Cases 213. (Referred to in quotation.) 11

Neumann v. *Commissioners of Inland Revenue,* (1934) A. C. 215; 18 Tax Cases 332 14

Commissioners of Inland Revenue v. *Pearson, and Commissioners of Inland Revenue* v. *Pratt,* 1936—2 K. B. 533 16

Whitney v. *Commissioners of Inland Revenue,* (1926) A. C. 37; 10 Tax Cases 88. (Referred to in quotation.) 10, 13

Miscellaneous

British Income Tax Codification Committee Report, Volume I 6, 7, 9, 13, 15, 17

Historical Note on Taxation at the Source by Board of Inland Revenue 8

Treatise on the Law of Income Tax (Great Britain), Shaw & Baker, London, 1937..... 8

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Reasons for Filing Brief

1. The attorneys filing this brief are attorneys for F. W. Woolworth Co., the plaintiff-appellant and the petitioner in *F. W. Woolworth Co.* v. *United States,* which is now pending before this Court under Docket No. 568, October Term 1937, on a petition for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit.

2. The principal issue involved in the Woolworth case is the sole issue involved in the Biddle case, namely, whether credit may be taken by the shareholder on account of the British income tax deducted and withheld from English dividends. The Circuit Court of Appeals, Second Circuit, in its opinion in the Woolworth case has adhered to and restated its decision in the Biddle case, and the two cases are closely related.

3. The record in the Woolworth case contains important British tax exhibits, namely, photolithographic reproductions of British income tax forms, which are not available in the Biddle case and which may be of practical assistance to this Court in determining the issue.

4. Apart from the immediate interest of the private litigant represented by the undersigned attorneys, the Biddle case presents a question of substantial public importance. The decision of this Court will affect the right of every American citizen or domestic corporation owning a share of British stock. Out of their long association with this problem, the undersigned attorneys desire to bring certain general considerations to the attention of this Court as bearing on the issue.

The Issue and The Precedents

The Question:

> *Is the British income tax, which (under authority of the British income tax statute) is deducted and withheld on the payment of an English dividend, an income tax which is paid by the shareholder receiving the dividend, as distinguished from the corporation paying it, so as to constitute an allowable credit against the United States income tax under the credit sections of the United States income tax statutes?*

The Precedents:

Administrative Practice:

From the effective date of the Revenue Act of 1918 until late in 1933 the Commissioner of Internal Revenue, as a matter of administrative practice consist-

ently allowed credit on account of such income taxes to the shareholder and issued several important published rulings to that effect. In the Woolworth case the Commissioner actually made large refunds of overpayments based on the allowance of this credit, and did not raise an issue respecting it until after the Woolworth suit was brought on other issues.

Circuit Court Decisions:

Five decisions on this question have been handed down to date by the Circuit Courts of Appeals (including the cases now at bar):

1. *Welch, Collector* v. *St. Helens Petroleum Co., Ltd.* (C. C. A., 9th), 78 Fed. (2d) 631.

This case was tried on a stipulation which makes no reference to the British Tax Act or decisions and the British statute was not before the trial court. The Circuit Court of Appeals in its decision holding that the shareholder does not pay the tax largely relies on the English decision in the Neumann case, commented on below, *infra* 14, which as shown, does not establish the controlling law. On the meagre record before the Court in the St. Helens Petroleum Co., Ltd. case, its decision cannot be regarded as of first importance.

2. *Mary Duke Biddle* v. *Commissioner of Internal Revenue* (C. C. A. 2nd), 86 Fed. (2d) 718 (the instant case); and
3. *F. W. Woolworth Co.* v. *United States* (C. C. A. 2nd), 91 Fed. (2d) 973.

In these two cases the Second Circuit held that it accepts the testimony of the British tax expert in the Biddle case

that under the British system the shareholder pays the tax, but refused to allow the credit on the ground that the tax is not "paid" within the meaning of our statute. The Biddle case affirmed 33 B. T. A. 127, on this issue, and the Woolworth case reversed the decision of the District Court for the Southern District of New York, 15 Fed. Supp. 679.

4. *United Shoe Machinery Corporation* v. *White, Collector, etc.* (C. C. A. 1st), 89 Fed. (2d) 363.

In this case the First Circuit held that while the tax is assessed against the English corporation, in fact and in law it is required to fall and does fall on the shareholder, and therefore constitutes a tax paid by the shareholder. The Court specifically refused to follow the decision of the Second Circuit in the Biddle case.

5. *George W. Elkins* v. *Commissioner of Internal Revenue* (C. C. A. 3rd), 91 Fed. (2d) 534, reversing 33 B. T. A. 127.

In this case the Third Circuit also specifically refused to follow the Second Circuit decision in the Biddle case, and, in the opinion of Judge BUFFINGTON, held that the only question with which the Court is concerned is:

> "Did the petitioner pay the income tax, and to ascertain this we must see what has happened in England; what kind of a tax was paid; who paid it?"

The Court concludes:

> "There, we must find as a *fact* it is income tax paid by deduction or otherwise 'by the shareholder.'" (Italics are those of Court.)

Except in the St. Helens Petroleum Co., Ltd., case (which, as shown above, we do not regard as authoritative irrespective of its result), the Circuit Courts are in agreement that under the British income tax system the shareholder pays the tax. It is notable that the Second Circuit in its restatement of its position in the Woolworth case still adheres to this conclusion, notwithstanding that it refuses to find that credit is allowable. The issue is accordingly largely reduced to the more restricted question as to whether, in determining the incidence of the British income tax, the admitted foreign income tax law shall control.

Summary of Argument

POINT A. Under the British Tax System the Shareholder Pays the Tax Deducted and Withheld on the Payment of a Dividend.

1. The British System of Taxation.
2. Taxation of Dividends.
3. Neumann v. Commissioners of Inland Revenue.
4. British Administrative Practice.

POINT B. The Broad Relief Purposes of the Statute Require that the Credit be Allowed.

CONCLUSION.

(Discussion of decision in Biddle case.)

POINT A

Under the British tax system the shareholder pays the tax deducted and withheld on the payment of a dividend.

1. *The British System of Taxation:*

The question before the Court revolves around the British tax system. The particular statutory provisions will have been called to the attention of the Court in the major briefs. We propose herein to deal briefly with certain general considerations, and also, believing that it may be of great practical assistance to the Court, we shall quote from that section of the recent authoritative report of the British Income Tax Codification Committee*, which relates to the taxation of dividends. The Income Tax Codification Committee is a standing committee appointed by Hon. Winston Churchill, Chancellor of the Exchequer in October, 1927, for the purpose of codifying the British law relating to income tax, which has with British thoroughness been making an exhaustive study of the entire question, including statutory law, case law and administrative practice.

The British tax system must of necessity be considered in the light of its historical background. Income tax in Great Britain was first imposed in 1799 by a statute introduced by the younger Pitt to meet the cost of the Napoleonic Wars. This Act was repealed in 1802, but income tax was reintroduced in 1803 and again imposed by the statute of 1806. After Waterloo the tax was dropped and was not re-

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*The official title is "INCOME TAX CODIFICATION COMMITTEE REPORT", Volume I, Report and Appendices, Presented to Parliament by the Financial Secretary to the Treasury by Command of His Majesty April 1936; printed and published by His Majesty's Stationery Office.

vived until 1842, when Sir Robert Peel was Prime Minister. The report of the Codification Committee states that the Income Tax Act, 1842, was to all intents and purposes a reprint of the Act of 1806, with a few alterations and additions "relating to such novelties as railways, gas works and the tithe commutation rent charge, all of which had come into existence in the interval." The Act of 1853 continued to be the basic law until the passage of the Income Tax Act, 1918, which was intended to consolidate the two main statutes of 1842 and 1853 and to bring within one framework the succeeding legislation. The report in question describes the present statute as follows:

> "This Statute therefore, which at the present time is the principal Income Tax Act, is mainly a reproduction of a body of law enacted more than a century and a quarter ago and adapted to the economic, social and commercial conditions of that time."*

It is also necessary in considering the British tax system to bear in mind that it contains language and provisions which are described by this report as "antiquated and anomalous".

The British tax system differs materially from the American system, both in the quaint language in which the statute is framed and the conventions the statute employs. Thus, for example, while income of one year is charged with the tax, the measure of the tax is determined by the income of the preceding year. But the great distinguishing characteristic is that for purposes of the ordinary tax (roughly corresponding to our normal tax) the British system revolves around collection at the source. The gen-

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*P. 10 Income Tax Codification Committee Report, Vol. I.

eral scheme of the Income Tax Acts is, as far as possible, to collect income tax at the source, *i. e.,* to assess the person paying the income in respect to the income tax appropriate thereto. The person paying income tax has in general the right to recoup himself when making a payment of income to the person entitled thereto, by deducting and retaining the tax appropriate to that income.* This system has been well summarized by the Board of Inland Revenue as an income tax system which has been developed and founded on

> "* * * the great principal of taxation at the source, a principle which has lasted with many extensions and some notable recent exceptions to the present day, and has proved of such central importance in income tax administration that Professor Seligman, of Columbia University, U. S. A., has recently called it 'perhaps the chief cause of the great success of the English income tax'."**

There is a further distinguishing feature which appears to have been lost sight of by the Court below, and the failure to consider which gives rise to false analogies. Under the American system there is a clear cut differentiation between corporations as such and individuals, and each is taxed under separate specific sections of the taxing statute. No such differentiation appears in the English stat-

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*The Law of Income Tax, Shaw & Baker, London, 1937.

**Historical Note on Taxation at the Source by the Board of Inland Revenue, Reprinted at pages 152-155 in an Appendix to a Report entitled *Income Tax in Great Britain,* prepared in 1928 for the Joint Committee of Internal Revenue Taxation by Andre Bernard and published pursuant to House Resolution 195 as House Document No. 332, 70th Congress, 1st Session.

utes, and in fact corporations are not taxed as such but come within the category of "body of persons", which, as shown below, has an historical derivation antedating the rise of the corporation system. Moreover, there is no provision in the British statute specifically exempting dividends from the ordinary tax, whereas, in the American statutes, prior to the recent act, specific statutory credit was allowed against the net income for normal tax purposes on account of dividends, so that dividends were exempted from the normal tax. The medieval and modern concepts which separately underlie the two great systems show the fallacy of endeavoring to measure one by the other.

2. *Taxation of Dividends:*

The present contention of the Government that the shareholder does not pay the tax, and that the tax deducted is merely a recoupment by the corporation of a corporation income tax, is not sustained by the reasoned conclusions of the Income Tax Codification Committee, which devotes a special subsection to the question of taxation of dividends.*

In its Report the Committee states:

> "The original Statute of 1842 (1) contained no special reference to such dividends, except a most exiguous and by no means lucid one in section 54, which, after providing that the profits of companies, whether incorporated or unincorporated, were to be computed 'before any dividend shall have been made thereof to any other persons', enacted that all such other persons should allow out of such dividends, 'a proportionate deduc-

*Subsection 10, Dividends, Pages 61, et seq., of Report.

tion in respect of the duty so charged.' In the Consolidating Act of 1918 this enactment was reproduced in slightly different phraseology by General Rule 20, which runs:

> 'The profits or gains to be charged on any body of persons shall be computed in accordance with the provisions of this Act on the full amount of the same before any dividend thereof is made in respect of any share, right or title thereto, and the body of persons paying such dividend shall be entitled to deduct the tax appropriate thereto.'

"The Act of 1918 contains no other provision dealing specially with such dividends.

"There can be little doubt that all such dividends would fall, in principal, within the charging words of Schedule D of the Acts of 1842 and 1918 as 'profits from property,' and so it was declared by the House of Lords in *Whitney* v. *Commissioners of Inland Revenue* (2). But, so far as concerns the actual assessment and collection of tax, the practice from 1842 onwards was to treat companies on the lines of large partnerships, and to regard the dividends paid to shareholders as distributions of profits which had already paid tax in the hands of the company, and the shareholders (like partners) as immune from further taxation in respect of the sums so distributed to them. This view would not only be suggested by the terms of section 54 of the Act of 1842 (1), but by the legal view prevalent at the period as to the nature of the companies in question.

"Section 54 was, however, framed many years before the Joint Stock Companies Acts, and incorporated and unincorporated companies are referred to in it without

1. 5 & 6 Vic., c. 35.

2. [1926] A. C. 37; 10 Tax Cases 88.

distinction. It is worthy of note, as illustrating the then prevalent legal theory, that the first edition (published in 1860) of so well-known a legal text book as *Lindley on Companies* treated the subject as a branch of the law of partnership and was, indeed, entitled *A Treatise on the Law of Companies considered as a branch of The Law of Partnership.*

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"The principle upon which the taxation of dividends was administered from 1842 onwards, and up to 1930, is set forth in the Case Stated, and was sanctioned by the Court, in *F. H. Hamilton* v. *Commissioners of Inland Revenue.* (2) The Case Stated deals with the practice as follows:

> 'It is, and always has been, the almost universal practice to deduct from the gross amount of the dividend the tax appropriate to that amount, or, if the dividend is declared to be "free of tax", to treat it, for the purposes of computing total income, as equivalent to the gross amount which, after deduction of the appropriate tax, corresponds to the net amount actually paid, without any reference to the amount of the company's "statutory" income. This method of dealing with dividends is one of the accepted conventions under which the Income Tax Acts are regularly administered, and it is consistent with the actual words of the Acts * * *. An exception to the general rule has, in recent years, been admitted in a few special cases, where it has been clear that the payment of a dividend was, in whole or in part, a distribution of profits which, by reason of their capital nature, were not within the charge to income tax.'

2. [1931] 2 K. B. 495 at pages 502 and 503; 16 Tax Cases 213 at pages 219 and 220.

"The idea that the company's power of deducting tax from dividends was simply a power to pass on to its shareholders its own tax on its own income, resulting, as it would have done, in a company deducting as tax from its dividends an amount representing tax at a smaller or greater rate than that in force for the year, or being unable to deduct any tax at all, and in elaborate inquiries into the past history of the company's income and its accumulation, was thus never acted upon.

"So also, dividends were always treated as part of a taxpayer's income from all sources for the purpose of claiming exemption, and returnable accordingly as being 'annual payments' liable to deduction of tax. They were similarly, without question, treated as 'annual payments' charged to income tax under Schedule D in claims by charities for exemption from tax under section 105 of the Income Tax Act, 1842 (1) (now incorporated in section 37 of the Income Tax Act, 1918). The speech of Halsbury, L. C. in the case of *Attorney-General* v. *Ashton Gas Company* (2) well illustrates the then prevalent view that (whatever the method of collection) dividends of companies were taxable income. It is indeed difficult to imagine, from a common-sense standpoint, a receipt which is more obviously income.

"In 1910 super-tax was introduced, and the inclusion of dividends in the content of 'total income from all sources' became a matter of moment to taxpayers whose means enabled them to test the matter by litigation. Thus (to mention only a few cases) in *Brooke* v. *Commissioners of Inland Revenue* (3) the bold contention was put forward that, having regard to the taxation of dividends through the medium of the company's

1. 5 & 6 Vic., c. 35.
2. [1906] A. C. 10, at pages 11-13.
3. [1918] 1 K. B. 257; 7 Tax Cases 261.

profits, a dividend was not returnable as part of total income at all, i. e., as income of the shareholder. This view was rejected by the Court of Appeal, and their decision on this point was subsequently approved by the House of Lords in the case of *Whitney* v. *Commissioners of Inland Revenue.* In the course of the *Brooke* case the observation was made that a company deducting tax from dividends did so as agent for the shareholder. This view of the situation was, however, qualified a few years later by the view expressed in Lord Cave's speech in *Commissioners of Inland Revenue* v. *Blott* (5) as follows:

> 'Plainly, a company paying income tax on its profits does not pay it as agent for its shareholders. It pays as a taxpayer, and if no dividend is declared the shareholders have no direct concern in the payment. If a dividend is declared, the company is entitled to deduct from such dividend a proportionate part of the amount of the tax previously paid by the company; and in that case the payment by the company operates in relief of the shareholder. But no agency, properly so called, is involved.' "

The Report then continues a discussion of certain amendments, and, after referring to an amendment made by the Finance Act of 1927, making it clear that the rate at which tax could be deducted was the rate in force when the dividends became due, the Report states:

> "* * * This provision removed any doubt as regards the rate at which tax should be deducted when the company's year for which a dividend was paid was partly in one tax year and partly in another, and made

5. [1921] 2 A. C. 171, at page 201; 8 Tax Cases 101 at page 136.

it clear that it is unnecessary, if the rates of tax for the two tax years differ, to work out a proportion and to deduct tax at an intermediate rate. It had the result of putting a statutory seal to the view adopted in practice, that the power to deduct tax from dividends was not simply a power to pass on to shareholders the amount of the tax borne by the company upon its income."

3. *Neumann* v. *Commissioners of Inland Revenue*:*

The Court below in the Biddle case refers to, and the Government throughout the argument of these cases has relied heavily on the English decision in the Neumann case, as apparently establishing the proposition that the shareholder does not pay the tax, although it was correctly pointed out by counsel for the taxpayers that the Neumann case was a peculiar case arising under special circumstances and did not establish controlling principles of law on the general question. In the Neumann case certain income had not been subject to tax in the hands of the corporation which paid the dividend for the reason that the corporation was charged with a tax under Schedule A on the annual value of its realty holdings and the actual profits exceeded these Schedule A values, which were the basis of its income tax. On the distribution of the excess amount over the profits which had been subject to tax, the question at issue was whether the dividend was taxable on the gross amount before the deduction of the tax or on the net amount the shareholder received. Under the exceptional circumstances in that case the House of Lords held that tax could not be added to the dividend in order to arrive

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*[1934] A. C. 215; 18 Tax Cases 332; printed as Defendant's Exhibit Q in Woolworth case, R. 629.

at the amount of the shareholder's income from that source. The dividend paid in the Neumann case is wholly distinguishable from the dividend received by the shareholder in the Biddle case, for in the Neumann case the English corporation was taxed under Schedule A and distributed profits which had escaped the charge of the tax and were subject to tax in the hands of the shareholder only in the net amount, whereas, in the Biddle case the English corporation was taxed on its business profits under Schedule D and the dividend received constituted a distribution of these profits on which the tax was withheld at the source, and as to which there was no question that the amount of the tax must be added to the net amount of the dividend for purposes of determining surtax income.

The Codification Committee Report refers to the Neumann case under the section relating to dividends in detail. After completing its summarization of the case the Committee states:

> "We have felt great difficulty as to how the decision on this cross-appeal should be dealt with in a codifying measure In the first place, the grounds on which the Lords of Appeal based their opinions differed; Lord Tomlin considered that 'it would be repellent to most minds that the appellant should be charged as a part of his income with a sum which not only has never come to him but has never existed in fact'; Lord Warrington adopted Lord Tomlin's reasoning; Lord Wright, on the other hand, based his opinion chiefly on the use of the word 'net' in section 33 of the Finance Act, 1924."

The Report concludes that it does not attempt to give statutory effect to the decision because of the reasons stated, although it points out that its proposals will alter

the law in its application to the "peculiar circumstances" of the Neumann case. That is, the Codification Committee deliberately refuses to adopt the principle laid down in the Neumann case, and from its statements respecting this case it is clear that it can be of little, if any, assistance in determining the present issue.

In two recent cases, *Commissioners of Inland Revenue* v. *Pearson,* and *Commissioners of Inland Revenue* v. *Pratt,* 1936—2, K. B. 533, the Court, on the solicitation of the Crown, also refused to follow the Neumann case in the solution of the problem before it. In the first of these cases the English company in paying a dividend had expressly refused to exercise its statutory option of deducting the tax. It was argued for the taxpayers that under the Neumann case only the net amounts could be subject to tax, but, on the appeal, the Crown urged that the decision in the Neumann case was "decided on peculiar facts" and that if this decision stood, the English surtax could easily be defeated. The Court in sustaining the Crown said:

> "The companies in paying income tax under Schedule D out of their profits Pound for Pound, and subsequently declaring dividends which absorb only the remainder or part of the remainder of their profits were in effect deducting income tax, or, as Buckley, J., said in the Ashton Gas Co. case, relieving the shareholders from liability."

The Ashton Gas Co. case* (Plaintiff's Exhibit No. 55, R. 327, Woolworth Record), is one of the authorities on which plaintiff relies therein. The Pearson case establishes that the point on which the Government placed so much

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*1906 A. C. 10.

emphasis in its argument below in the Biddle case, namely, that the right to deduct the tax was merely optional, is entirely illusory, for whether the option is exercised or not, the British law as thus interpreted requires that the shareholder be taxed for surtax purposes on that sum which if the tax were deducted at the rates in force would produce the net dividend received. We are unable to conceive how clearer proof on this question could be submitted than this development.

4. *British Administrative Practice:*

In determining this issue, both the Government and the Court below have strangely failed to give adequate recognition to British administrative practice. That this is one of the great sources of the British tax system is set forth in the Report of the Codification Committee, which refers to it as follows:

> "* * * In addition there is the practice of the Inland Revenue Department, which, over a long tract of time, has evolved and stereotyped numerous administrative expedients to deal with cases for which the law has made no detailed provision or where the law is obscure and ambiguous. Much of this practice has now engrained itself in the administration of the Statutes and having been generally accepted has acquired an authority of its own. A large body of material of this nature has thus had to be taken into consideration by the Committee.*

In the Woolworth case the plaintiff assembled for the information of the Court a large body of actual English

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*P. 12 Income Tax Codification Committee Report, Vol. I.

tax forms used in administrative practice, which appear in the Woolworth record, reproduced in photolithographic form as Plaintiff's Exhibits 38 N to Z and 38 AA to II, beginning at page 384 and continuing to page 435. The trial court in its special finding of fact found with respect to these exhibits as follows:

> "During the years involved herein, forms and instructions were promulgated by the English Commissioners of Inland Revenue in conformity with which an English taxpayer is required in both his income tax and super-tax returns to include in his taxable income the gross amount of his dividends received, and the tax is computed on the amount so reported. If by reason of losses, reliefs or deductions the taxpayer is subject to no tax, the tax deducted from dividends paid by him is refunded in full by the English Government. If his tax liability so computed is less than the amount of tax deducted from his dividends, the excess of the tax so deducted over the tax liability is refunded to him by the English Government."*

Believing that these forms are of first importance in a question of this character, we respectfully call this Court's specific attention to the following exhibits:

> *Income Tax Returns* (Plaintiff's Exhibits 38, N to Q, Woolworth Record, pp. 384-394).

In these returns the taxpayer is required to include the gross amount of all dividends received. At top of page 3 is a statement:

> "The claimant must set forth every source of his income with the amount derived from each source,

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*Special Finding of Fact No. 18, Fol. 2783, R. 928, Woolworth Record.

whether returned elsewhere for assessment or not, whether tax has been paid on it or not, and notwithstanding that the income may have been received 'free of tax' or 'tax compounded.'"

Instructions Relating to the Income Tax Returns (Plaintiff's Exhibits 38, R to W, Woolworth Record, pp. 396-410).

On page 4 appears the following statement:

"Dividends received 'free of tax' or interest on 'tax compounded' British Government securities should be entered in part (i) or space (e) on page 3 and treated as if the amount actually received represented net income after deduction of tax. The gross amount corresponding to the net amount received being entered; thus, if the amount actually received 'free of tax' or 'tax free' were £10 and the current income tax rate were 6s. in the pound the amount to be entered would be £14.5.8 this being the gross amount which after deduction of tax, would leave a net income of £10."

Supertax Returns (Plaintiff's Exhibits 38, X to Z, Woolworth Record, pp. 412-418).

Under the "Notes", the taxpayer is required to report "Income chargeable with income tax by way of deduction", and page 2 of the "Directions" contains instructions as to the amount returnable as dividends "whether the income is received 'less income tax' or 'free of income tax.'"

As in the income tax returns, under "dividends", it is required to report:

"Gross amount of income taxed before receipt including dividends paid 'free of tax.'"

Refund Claims (Plaintiff's Exhibits 38, dd, ff and hh, Woolworth Record, pp. 424, 428 and 432).

These require similar information with regard to dividends, with separate columns for "Amount of income before deduction of tax", and "Amount of income tax paid on or deducted from each source of income."

Instructions Accompanying the Claims for Refund (Plaintiff's Exhibits 38, cc, ee and gg, Woolworth Record, pp. 422, 426 and 430).

These set forth specific examples on the back of the forms. In each example the taxpayer is assumed to have received a certain sum as "gross income from dividends before deduction of income tax". The form refers to the tax deducted from these dividends as *"A has paid tax on* * * *", the amount of the dividend.

The exhibits thus before the Court in the Woolworth case establish incontrovertibly that for all the many purposes of the British income tax administration the authorities charged with the administration of the tax deal with the tax withheld from dividends as a tax paid by the shareholder by deduction.

POINT B

The broad relief purposes of the statute require that the credit be allowed.

The credit sections* of the American statute have been before this Court on only one occasion (*Burnet* v. *Chicago Portrait Co.*, 285 U. S. 1, 76 Law Ed. 587), but on that occasion this Court in elaborate footnotes carefully reviewed the

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*As the pertinent provisions will be before the Court in the major briefs, they are not quoted in this brief. See generally 26 U. S. C. A. 113, Supplement C—Credits Against Tax.

legislative development of this provision, and in its opinion recognized that the primary design of the provision was "to mitigate the evil of double taxation". The Chicago Portrait Co. case presents a close analogy to the Biddle case. In the Chicago Portrait Co. case, income tax had been paid to New South Wales, a component State of the Commonwealth of Australia, and the Government sought to defeat the credit on the narrow technical ground that the tax had not been paid to a "foreign country" within the meaning of the statute. This Court rejected this method of rigid interpretation and held that the broad purposes underlying this relief section required the allowance of the credit, even though New South Wales did not have the juridical status of an independent foreign country. In the Biddle case the Government, again ignoring the broad purposes and the general scheme of this section of the statute, seeks to defeat its application in the instant case on the narrow technical ground that the tax was not "paid" within the meaning of our statute. On the authority of this earlier decision this Court should reject the Government's contention, for the situations are in fact parallel.

Under the Corporation Tax of 1909, and the Revenue Acts of 1913, 1916 and 1917, no relief was allowed on account of foreign income taxes, except as a *deduction* from gross income. In 1918 Congress recognized the problem growing out of the double international taxation of the same source of income and first adopted the credit provision, this being done under two separate sections, one of which allowed credit in the case of individuals and the other in the case of corporations. It is noteworthy that when Congress first recognized the urgency of this problem it did not limit the operation of the credit provision merely to American tax-

payers who paid income taxes abroad, but it took a further step in the case of domestic corporations owning foreign subsidiaries and provided that in such cases the domestic corporation should be allowed a proportionate credit against its own income tax on account of the foreign income tax paid by its subsidiary. In the face of this provision, which allows credit for a tax never paid by the domestic corporation, and having no direct relation, as does the English tax, to the domestic corporation, the reasoning of the Court below that Congress did not intend these relief provisions to operate where the tax was not actually paid within the meaning of our statutes, seems entirely without force or point.

From 1918 to 1937 Congress has unfalteringly maintained the integrity of the credit relief sections. Such amendments as have been made have been by way of clarification, as in the consolidation of the two separate sections in the Revenue Act of 1928, or by way of limitation, to insure that the credit shall not exceed the American income tax which would have been payable, as in the case of the enactment of subdivision (b) of the Revenue Act of 1928. This is clearly established by such developments as the following:

(a) In Section 213 (b) 14 of the Revenue Act of 1926 (which has been continued in the later acts and now appears as Section 116 (a) of the Revenue Act of 1936, 26 U. S. C. A. 116), Congress went beyond the mere credit provision in order to insure relief and provided that where an individual citizen of the United States was a *bona fide* non-resident of the United States for more than six months during the taxable year, and received from sources without the United States earned income, then such earned income

was specifically exempt from taxation under our statute. That is to say, Congress in this case recognized that the credit for foreign income taxes on such earned income theretofore allowed was not sufficient and granted complete exemption.

(b) In House Report No. 350, 67th Congress, 1st Session, relating to the Revenue Act of 1921, page 8, the Committee on Ways and Means proposed in substance under certain conditions to tax American citizens or domestic corporations, in the same manner as non-residents, that is, only on income derived from sources within the United States. In such cases this would have completely eliminated foreign dividends from tax, whether on gross or net basis, and, as pointed out in the footnote* to the Chicago Portrait Co. case opinion, even though this change was not adopted, it shows the clear Congressional intent.

(c) The preliminary report of the Subcommittee on Ways and Means, 73rd Congress, 2nd Session, page 9, relating to the Revenue Act of 1934, in line with the urgent need for revenue at that time, recommended the elimination of the foreign credit provision and the return to the former deduction basis of treating this problem. The Senate, on the recommendation of the Treasury Department, opposed this House proposal, and the final result was a recession by the House and the continuance in the 1934 Act of the former credit provisions.

(d) Over this entire period the question of double international taxation has received increasing international at-

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*285 U. S. 9, 76 L. ed. 592.

tention. A uniform code of principles for eliminating double taxation was adopted in 1929 at the Congress of the International Chamber of Commerce meeting at Amsterdam.* These international developments were reflected in proposed legislation, which was introduced in Congress in 1930 by Mr. Hawley, Chairman of the Ways and Means Committee, as H. R. 10165, under the caption "A Bill to Reduce International Double Taxation". This Bill embodied proposals made by the Treasury Department after a careful study of the problem, and, although not enacted, it unquestionably influenced later developments. The Revenue Act of 1936, under Section 22 (b) (7), 26 U. S. C. A., 22 (b) (7), contains a new provision which specifically exempts the following income from taxation:

> "Income Exempt under Treaty.—Income of any kind, to the extent required by any Treaty obligation of the United States".

Two treaties on the subject have been concluded, ratified by the Senate, and are now in force, to wit:

1. The Convention and Protocol with France, proclaimed by the President on April 16, 1935. (T. D. 4746, Vol. XVI, Internal Revenue Bulletin No. 29, July 19, 1937.) Under

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*A study of the problems of international taxation is reported in "Taxation of Foreign and International Enterprises, France, Germany, Spain, the United Kingdom and the United States of America"—League of Nations, Geneva, 1932. An article by Mitchell B. Carroll (American representative at the international conference) appears in National Income Tax Magazine, Volume VII, No. 4, page 132, April 1930, and quotes Mr. Ogden Mills to the effect that double taxation is a barrier to the expansion of international trades and investments.

this treaty certain income, including dividends, received by the resident nationals of one contracting country is exempt from the income tax imposed by the other contracting country.

2. The Reciprocal Tax Convention between the United States and Canada, ratified August 13, 1937. (Vol. XVI, Internal Revenue Bulletin No. 42, October 18, 1937.) Under this treaty both nations agree that the residents of the other shall not be taxed, except at the same rate of tax, which, in view of the lower tax rate in Canada, has the effect of limiting the United States income tax withheld from dividends paid to Canadian residents.

In the face of this long legislative record, it cannot be argued that even the necessity of the revenue has made Congress indifferent to this principle, nor can it be believed that Congress intended that these provisions should become inoperative in their most important foreign quarter, namely, Great Britain, because of a technical construction of the one word "paid".

Finally, on this point, we refer this Court to Section 103 of the Revenue Act of 1936 (26 U. S. Code, Annotated, 103, first enacted as Chapter 277, Section 103, 48 Stat. 703, on May 10, 1934), under which it is proposed that whenever the President finds that, under the laws of any foreign country, citizens or corporations of the United States are being subjected to discriminatory or extra-territorial taxes, the President shall so proclaim, and the rates of tax then in force shall be doubled in the case of each citizen and corporation of such foreign country. This measure further shows the keen desire of Congress to protect the American

taxpayer in the matter of international taxation, and we submit that it is not conceivable that if Great Britain should raise the rates of withholding in the case of dividends paid to American shareholders, it would be held by our Courts that the discriminatory act of Great Britain did not come within the compass and scope of this protective legislation, on the ground that the American shareholder does not pay the tax!

To hold that credit may not be allowed in this case is in substance to render these broad relief provisions of no avail in the most important field of their operation.

Conclusion

1. Two fundamental errors pervade the decision of the Court below, either of which is fatal to its judgment:

(a) The Court errs in holding that the question at issue must be resolved not by the foreign law, which imposes the tax, but under our principles and system of taxation. No adequate supporting authority for this proposition is given by the Court. The St. Helens case, to which it refers, as shown above, rests on the English decision in the Neumann case, and is not authoritative. The further case it cites, *Shearer* v. *Commissioner*, 48 F. (2d) 552, is not in point, for that case involved a purely domestic tax question and related to an excise tax, which by statute was imposed on the dealer and collected by him on the sale of the article from the customer as a matter of private contract.

(b) Accepting the principle laid down by the Court below that the word "paid" must be fitted into the mold of our own system and not the British, the Court is not

correct in its conclusion that if a similar tax were withheld under our statute, the shareholder would not be regarded as the taxpayer. Under our well grounded principle of constructive receipt and payment (the basis of huge assessments), neither our Courts nor our administrative officials would have any difficulty in sustaining taxation on the gross amount in the same manner as the British have done in the case of the surtax. If, for example, the Federal income tax was on the basis of the "gross receipts" (as is the City of New York income tax), it can well be imagined that the Treasury Department would have no difficulty in sustaining the inclusion of the gross dividends. The Court below is unable to give authority for its conclusion on this point, and its reasoning is not persuasive. The question is one of ultimate statutory liability and not of mere "burden", a distinction which the Treasury Department itself has recognized.*

2. There is ample precedent for the necessary principle that in the construction of a foreign income tax law, when questions arise under the provisions of our own income tax law, we must look to the terms of the foreign statute. The Court below correctly did this very thing in its earlier decision in *United Dyewood Corporation* v. *Bowers,* 56 Fed. (2d) 603, in which the credit was allowed, and it was in fact required also to consider the British statute in deter-

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*Article 143-9, Regulations 94, Income Tax (dealing with the withholding provisions of the Revenue Act of 1936), provides:

"Tax withheld at the source upon fixed or determinable annual or periodical income paid to non-resident alien fiduciaries is deemed to have been paid by the persons ultimately liable for the tax upon such income."

mining questions in the Woolworth case relating to credit for Schedule D income taxes under Section 238 (e) of our statute. This principle is also fully established by the cases cited in the appellant's major brief. To permit any other method of interpretation to be applied would involve these matters in hopeless confusion, for the right to credit would not depend on the terms of the statute but on the particular view an official might take as to the comparative relation between the foreign statute and the American system. Conceivably, we can no more expect correctly to determine the effect of the foreign law by injecting into its interpretation the statutory language of our own law than we could hope to establish that London is the capital of the British Empire by considering the geographical fact that Washington is the capital of the United States.

3. Finally, we submit that the national interest does not support the position of the Government in these cases. The question rises far above the importance of the immediate amount of revenue or refund here involved. The purpose of the statute is to promote public good at the partial expense of the public revenue. The statute recognizes that if we are to prosper as a nation, we must send our citizens and our capital abroad, and this we cannot do if our citizens or our capital are subjected to the crushing load of double international taxation, especially at a time such as the present when everywhere rates reach points approaching confiscation. Nor has the revenue of the Government been injured by this wise policy. In the Woolworth case, for example, the success of the Woolworth English venture has brought great revenue to this country, and even if in the first instance the foreign dividends are relieved in part

from tax by the operation of the credit provisions, the foreign income flows into the coffers of our national income and yields substantial revenue. To deny the credit is plainly to defeat the statute, for after all argument dies away, the stark fact remains that the amount of the dividends which the American shareholder would otherwise receive *is reduced by the amount of the British dividend tax. The shareholder does in fact pay the tax.*

Respectfully submitted,

TOLBERT, EWEN & PATTERSON,
Amici Curiae,
45 Cedar Street,
New York, N. Y.

WARD V. TOLBERT,
JOHN L. MCMASTER,
BERTRAM F. BONGARD,
DOUGLAS H. THAYER,
of Counsel.